CORPORATIONS COMMITTEE
BUSINESS LAW SECTION
THE STATE BAR OF CALIFORNIA
180 HOWARD STREET
SAN FRANCISCO, CA 94105-1639
http://www.calbar.org/buslaw/corporations

A PUBLIC COMMENTARY

November 18, 2003

"At Every Peril"

New Pressures on the Attorney-Client Relationship

The Corporations Committee of the Business Law Section of the California State Bar (the "**Corporations Committee**") consists of attorneys who are engaged in regularly advising businesses and individuals in corporate and securities law issues. Members of the Corporations Committee include individuals who have formerly served as federal and state securities regulators. The Corporations Committee notes that increasing attention has been focused on the role of attorneys in corporate and securities transactions in light of several well-publicized allegations of fraud involving some of the country's largest corporations as well as the demise of a major accounting firm.

The Corporations Committee supports enforcement of federal and state securities laws and deplores misconduct by attorneys either in assisting clients to violate those laws or to cover up such violations. However, the Corporations Committee is concerned that recent regulatory and enforcement developments adversely affect the critical role of attorneys in corporate and securities transactions. These developments seriously undermine the value of preventative counseling and effective advocacy upon which our system of justice depends, rather than providing desired results.

This Public Commentary sets forth case law and other authority for the following points:

- Pressures by governmental authorities on clients to waive the long-standing protections of the attorney-client privilege, and work product doctrine are unproductive and may be contrary to public policy.

- Effective operation of our judicial system (as well as due process) requires that clients be able to communicate freely with their legal advisors without fear of disclosure.

- The roles and duties of attorneys and independent public auditors are fundamentally different.

1. Pressures on Clients to Waive the Protections of the Statutory Duty of Attorneys to Maintain Confidentiality, the Attorney-Client Privilege, and the Attorney Work Product Doctrine are Unproductive and may be Contrary to Public Policy.

The fundamental importance of the confidential relationship between client and attorney is well-recognized by the United States Supreme Court:

> The attorney client privilege is one of the oldest recognized privileges for confidential communications. *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981); *Hunt v. Blackburn*, 128 U.S. 464, 470 (1888). The privilege is intended to encourage "full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and the administration of justice." *Upjohn*, *supra*, at 389. ... Our interpretation of the privilege's scope is guided by "the principles of the common law . . . as interpreted by the courts . . . in the light of reason and experience." Fed. Rule Evid. 501; *Funk v. United States*, 290 U.S. 371 (1933).[1]

The California Supreme Court has similarly articulated the importance of protecting that aspect of the relationship:

> The attorney has a duty "[t]o maintain inviolate the confidence, and at every peril to himself or herself to preserve the secrets, of his or her client." (Bus. & Prof. Code § 6068, subd. (e).). ... "Protecting the confidentiality of communications between attorney and client is fundamental to our legal system. The attorney-client privilege is a hallmark of our jurisprudence that furthers the public policy of ensuring ' "the right of every person to freely and fully confer and confide in one having knowledge of the law, and skilled in its practice, in order that the former may have adequate advice and a proper defense." [Citation.]' [Citation.]" (*People ex rel. Dept. of Corporations v. SpeeDee Oil Change Systems, Inc.* (1999) 20 Cal. 4th 1135, 1146 [86 Cal.Rptr.2d 816, 980 P.2d 371] [the privilege is relevant in determining whether law firm should be disqualified].) "It is no mere peripheral evidentiary rule, but is held vital to the effective administration of justice. [Citation.]" (*Roberts v. City of Palmdale* (1993) 5 Cal. 4th 363, 380 [20 Cal.Rptr.2d 330, 853 P.2d 496].)[2]

In the past, the Securities and Exchange Commission (the "SEC") has recognized the importance of this confidential relationship and of the attorney-client privilege and the attorney work product doctrine which are based upon it:

> In some cases, the desire to provide information to the [SEC] staff may cause companies to consider choosing not to assert the attorney-client privilege, the work product protection and other privileges, protections and exemptions with respect to the [SEC].

> The [SEC] recognizes that these privileges, protections and exemptions serve important social interests.[3]

Recent rulemaking initiatives by the staff of the SEC and the Internal Revenue Service (the "IRS") appear to be in conflict with those interests.[4] Additionally, the Corporations Committee is concerned that pressure by the SEC and prosecutors on targets of government investigations to waive the statutory duty of attorneys to maintain client confidences, the attorney-client privilege, and the attorney work product doctrine undermines those "important social interests." The Corporations Committee is further concerned that targets are being pressured to waive these important protections in return for vague and ill-defined assurances of possible leniency and without a full recognition of the ultimate ramifications of such waivers.

(a) Report of Investigation Pursuant to Section 21(a); United States Department of Justice.

In October 2001, the SEC issued a "Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and SEC Statement on the Relationship of Cooperation to Agency Enforcement" (the "**21(a) Report**"). In the 21(a) Report, the SEC emphasized two points. First, it noted that large amounts of taxpayer and investor money could be saved when corporations undertake to investigate and remediate misconduct. Second, it announced a willingness to credit cooperative behavior, including waiver of client confidentiality protections, in deciding whether to take enforcement action.[5]

The United States Department of Justice has even more recently cited the waiver of the protections of the attorney-client privilege and the attorney work product doctrine as a factor to be considered in deciding whether to charge a corporation:

> One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure, including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel.[6]

(b) Waiver of the Attorney-Client Privilege or the Attorney Work Product Doctrine Can Have Significant and Far-reaching Consequences for the Client and the Public.

The Corporations Committee agrees that public interests are served when corporations self-investigate and remediate misconduct. However, emphasizing waiver of client confidentiality undermines the public interest that underlies the protections accorded to attorney-client communications -- particularly when such waivers are given at early stages of an investigation.

When allegations of possible misconduct arise, corporations can be subject to multiple types of lawsuits and related actions. At the federal level, alleged misconduct with securities law implications can be subject to administrative or civil enforcement action by the SEC as well as

criminal prosecution by the office of the U.S. Attorney.[7] The same alleged misconduct might also be subject to administrative or civil enforcement action as well as criminal prosecution by one or more states. In some cases, the alleged misconduct can result in disciplinary action by a self-regulatory organization. Finally, the alleged misconduct may engender one or more civil lawsuits brought by shareholders.[8] Moreover, the SEC often makes its files available to the U.S. Attorneys and state prosecutors.[9] Given the very real potential of multi-track enforcement, corporations face a serious dilemma when asked at a very early stage by just one regulator to waive client confidentiality protections. This is especially true when the regulator only provides vague assurances of possible leniency for "cooperation".[10] Moreover, assurances of leniency by one regulator do not bind other enforcement authorities or private litigants. In fact, lenient treatment by one regulator in exchange for waiving the privilege may be a very bad bargain when it is followed up by harsh treatment by another enforcement authority who may see little reason, much less an obligation, to reward cooperation with the first regulator.

The pressure can be even more acute when regulatory authorities conduct wide-ranging investigations of entire industries in response to allegations of misconduct by one or a few members of the industry.[11] Such investigations create a conundrum similar to the classic "prisoners' dilemma" because all members of the targeted industry may be better off if they preserve the privilege while conducting their own examination of facts and establishing their own legitimate defenses.[12] However, a corporation that waives confidentiality protections may be rewarded by investigators as "cooperative" while those not waiving the privilege may be targeted as "uncooperative". Consequently, waiver of client confidentiality becomes each corporation's dominant strategy and ultimately involves all targeted corporations waiving the privilege.[13] While enforcement authorities may complete more proceedings more rapidly by triggering this "rush to the exits" phenomenon, it comes at a very high cost to public policy: reinforcing the notion that the end justifies the means, even at the expense of well-established principles of justice and time-tested rules as to process.[14]

(c) What is the Unintended Result of Waiver?

Regardless of the efficiency of the outcome for the individual corporations facing regulatory or enforcement pressure to waive attorney-client confidentiality, the Corporations Committee believes that broader and more important public interests are at stake. An emphasis on waiver of client confidentiality protections by a single regulator as a factor in determining cooperation leads to unintended and troubling results, which can reduce the efficient operation of our system of justice. Over time, clients will anticipate that they may face a "prisoners' dilemma" in which their dominant strategy will be to waive attorney-client confidentiality. As a result, clients would become reluctant to consult proactively and fully with legal counsel about issues. Knowing that the enforcement authorities will be privy to all information developed in any self-investigatory process will also serve as a disincentive for clients to self-investigate and remediate or even as an incentive to use the self-investigation process to advocate rather than take a critical look at potential misconduct. Pressure on corporations to waive client confidentiality protections thus creates additional risks of harm to investors and innocent targets of investigation and, even to the public itself.

2. Our System of Justice Requires that Clients be able to Communicate Fully and Frankly with their Attorneys Without Fear of Disclosure.

The Corporations Committee recognizes that attorneys who advise publicly traded corporations and/or their controlling persons play a unique and often pivotal role under the federal and state securities laws. That role does not, however, include service as an adjunct or deputy to regulatory authorities in enforcing those laws.[15] Indeed, our adversarial system of justice cannot function as intended unless attorneys can act solely as advocates and advisers to their clients, separate and apart from the regulators enforcing those laws.

The importance of the assistance of counsel is grounded on common law principles and enshrined in the Sixth Amendment to the U.S. Constitution[16] (as to criminal trials) and reflected in the Administrative Procedure Act.[17] Indeed, the California Supreme Court has stated "the attorney-client privilege has been a hallmark of Anglo-American jurisprudence for almost 400 years."[18] The Corporations Committee is concerned that Rules which weaken the confidential and fiduciary relationship between counsel and client interfere with the attorney-client relationship and the client's right to effective assistance of counsel.

If attorneys are not legally obligated to keep their clients' confidences, clients will "mind their tongues" when seeking advice and counsel. A client cannot reasonably be expected to lay the full facts of its case before counsel if the client believes that, by doing so, it may well be creating evidence which could be used against it. When full and frank discussion is curbed, legal counsel will not have sufficient information to be able to provide the right advice or defend the client adequately. Public policy and the proper administration of justice require that clients may not be placed in the position of foregoing competent legal advice and defense out of fear that communications which are necessary to obtaining that advice and counsel will be subject to disclosure. As noted by the California Supreme Court:

> Protecting the confidentiality of communications between attorney and client is fundamental to our legal system. The attorney-client privilege is a hallmark of our jurisprudence that furthers the public policy of ensuring " 'the right of every person to freely and fully confer and confide in one having knowledge of the law, and skilled in its practice, in order that the former may have adequate advice and a proper defense.' [Citation]" (*Mitchell v. Superior Court* (1984) 37 Cal.3d 591, 599 [208 Cal.Rptr. 886, 691 P.2d 642].)[19]

The central importance of confidentiality to the quality of counsel is not new. Four hundred years ago, the famed lawyer and royal counselor, Francis Bacon, recognized the absolute necessity of confidentiality to good counsel:

> The greatest trust, between man and man, is the trust of giving counsel. For in other confidences, men commit the parts of life; their lands, their goods, their children, their credit, some particular affair; but to such as they make their counselors [sic], they commit the whole: *by how much the more, they are obliged by all faith and integrity.*[20]

The same public policies apply to corporate clients and not just to individuals, as the California Supreme Court has articulated clearly:

> Certainly the public policy behind the attorney-client privilege requires that an artificial person be given equal opportunity with a natural person to communicate with its attorney, within the professional relationship, without fear that its communication will be made public. As one writer has said, "The more deeply one is convinced of the social necessity of permitting corporations to consult frankly and privately with their legal advisers, the more willing one should be to accord them a flexible and generous protection."[21]

3. Independent Public Auditors and Attorneys have Fundamentally Different Roles and Duties.

A trend appears to be developing to treat the roles of attorneys and independent public auditors as similar and to apply the same principles of regulations equally to the relationship between each category of professionals and their clients. However, independent public auditors and attorneys fulfill fundamentally different roles and are charged with significantly different duties under relevant federal and state laws. The long-standing principles of public policy (and well-established case law interpreting and articulating them) support these distinctions. Such distinctions should be recognized and preserved by legislators, regulators and the courts. In particular, a "public watchdog" function is inherent in the role of independent auditors but is incompatible with the counseling and advocacy duties of attorneys. The Corporations Committee believes that importing the "public watchdog" or gatekeeper function into the role of the attorney would fundamentally impair the effectiveness of the attorney-client relationship and thus the benefits of it relied upon by our society, economy and judicial system: voluntary and informed compliance with legal requirements designed to protect those same sectors.

(a) Role of the Independent Public Auditor.

Auditors are required to be both objective and independent.[22] Although the client pays the auditor's fee, the auditor's responsibility "is not only to the client who pays his fee, but also to investors, creditors and others who may rely on the financial statements which he certifies. ... The public accountant must report fairly on the facts as he finds them whether favorable or unfavorable to his client. His duty is to safeguard the public interest, not that of his client."[23] This obligation to the public is recognized by the accounting profession's own standards of professional conduct:

> A distinguishing mark of a profession is acceptance of its responsibility to the public. The accounting profession's public consists of clients, credit grantors, governments, employers, investors, the business and financial community, and others who rely on the objectivity and integrity of certified public accountants to maintain the orderly functioning of commerce. This reliance imposes a public interest responsibility on certified public accountants. The public interest is defined as the collective well being of the community of people and institutions the profession serves.[24]

The importance of *independent* audits is evidenced by express statutory requirements in both the Securities Act of 1933 (the "**1933 Act**") and the Securities Exchange Act of 1934 (the "**Exchange Act**").[25] Moreover, the Exchange Act, the Public Utilities Holding Company Act of 1935, the Investment Company Act of 1940 and the Investment Advisers Act of 1940 each authorizes the SEC to require the filing of financial statements that have been audited by *independent* accountants.[26] Recently, Congress has reemphasized its concern regarding auditor independence with enactment of the Sarbanes-Oxley Act of 2002 (the "**Sarbanes-Oxley Act**").[27] Title II of the Sarbanes-Oxley Act entitled "Auditor Independence" added six new sub-sections to Section 10A of the Exchange Act specifically expanding, augmenting, or reinforcing existing concepts of "independence."[28]

Indeed, it is the act of certification of a client's financial statements that enlarges an auditor's responsibilities to third parties. As stated by Chief Justice Burger for the United States Supreme Court:

> By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a *public* responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public. This "public watchdog" function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust.[29]

(b) Role of Attorney As Confidential Adviser and Advocate.

Unlike an independent public auditor, an attorney does not *certify* or *attest*[30] aspects of his or her client's books or records. Rather, the attorney *interprets* for his or her client applicable legal standards and, on that basis, the client makes business and strategic decisions. Consistent with ethical standards and/or specific rules of court,[31] the attorney *advocates* for his or her client's position.[32] In other words, and as recognized by United States Supreme Court, the attorney is a confidential adviser and advocate and a loyal representative of his or her client.[33] Accordingly, the United States Supreme Court has recognized that attorneys generally cannot be held liable for "expertising" material in a registration statement in an action under Section 11 of the 1933 Act.[34]

The California Supreme Court has recognized that the imposition of duties to third parties would greatly impair an attorney's ability to serve the needs of his or her client:

> To make an attorney liable for negligent confidential advice not only to the client who enters into a transaction in reliance upon the advice but also to the other parties to the transaction with whom the client deals at arm's length would inject undesirable self-protective reservations into the attorney's counseling role. The attorney's preoccupation or concern with the possibility of claims based on mere negligence (as distinct from fraud or malice) by any with whom his client might deal "would prevent him from devoting his entire energies to his client's interests" (*Anderson v. Eaton* (1930) 211 Cal. 113, 116 [293 P. 788]). The result would be both "an undue burden on the profession" (*Lucas v. Hamm*,

supra, 56 Cal.2d 583, 589) and a diminution in the quality of the legal services received by the client. (See *Daly v. Smith* (1963) 220 Cal.App.2d 592, 604 [33 Cal.Rptr. 920].)[35]

(c) Distinction between Roles of Independent Public Auditors and Attorneys.

The distinction between the roles and responsibilities of independent public auditors and attorneys is underscored by the fact that Congress in enacting the Sarbanes-Oxley Act specifically prohibited a corporation's independent public auditor from providing it legal services or other expert services which are not otherwise subsumed within the audit process.[36] If independent public auditors and attorneys shared the same obligation of independence, this prohibition would make little sense. Implicit in this prohibition is recognition that attorneys are not expected or required to have the same type of obligation to the public that is required of independent auditors. Indeed, it recognizes that the prerequisite of confidentiality in rendering legal services would inhibit the *independence* of the public auditor providing such services.

The difference between the two roles is further illustrated by their different responsibilities with respect to client confidences. Consonant with the public responsibilities of independent auditors, Congress has mandated that in certain circumstances accountants acting in their capacity as independent public auditors report illegal acts to the SEC. In contrast, Congress did not do so for attorneys when it enacted the Sarbanes-Oxley Act.

Each California attorney, moreover, is required by statute to maintain his or her client's confidential information at "every peril to himself or herself".[37] The heavy burden imposed on members of the bar by this requirement is illustrated by the comments of Presiding Court of Appeal Justice Shinn who stated in a concurring opinion:

> The privilege of confidential communication between client and attorney should be regarded as sacred. It is not to be whittled away by means of specious argument that it has been waived. Least of all should the courts seize upon slight and equivocal circumstances as a technical reason for destroying the privilege. Here the attorney was compelled to testify against his client under threat of punishment for contempt. Such procedure would have been justified only in case the defendant with knowledge of his rights had waived the privilege in open court or by his statements and conduct had furnished explicit and convincing evidence that he did not understand, desire or expect that his statements to his attorney would be kept in confidence. *Defendant's attorney should have chosen to go to jail and take his chances of release by a higher court*.[38]

The California Evidence Code further requires that attorneys must assert the attorney-client privilege when the communication is sought to be disclosed.[39] In contrast, the regulations of the California Board of Accountancy make numerous exceptions to an accountant's duty to maintain client confidences, including disclosures made in response to an official inquiry from a federal or state government regulatory agency.[40]

In addition, both federal and state evidence rules protect attorney-client communications from discovery.[41] No similar privilege has been generally recognized for accountant-client communications, even when the accountant is not serving as an independent public auditor.[42]

Because effective legal counsel and advocacy requires full and frank communication, attorneys carry a heavy responsibility to maintain client confidences.

The SEC has stated that its rules of independence are predicated on, among other things, the principle that "an auditor cannot serve in an advocacy role for his or her client".[43] This principle of mutual exclusivity between independence and advocacy is equally applicable in the obverse: an attorney serving in an advocacy role for his or her client cannot in this context also be "independent" of that client in filling that role. Thus, the imposition of the "public watchdog" or "gatekeeper" function of auditors is incompatible with and inimical to the fundamental role and responsibilities of attorneys as advocates and counselors to their clients.

Indeed, Rule 3-310 of the California Rules of Professional Conduct prohibits a California attorney from accepting or continuing a representation when the attorney "has or had a legal, business, financial, professional, or personal relationship with another person or entity the member knows or reasonably should know would be affected substantially by resolution of the matter." The imposition of broad responsibilities to the public or government regulators would engender exactly the type of divided or shared loyalties that Rule 3-310 is designed to forestall.

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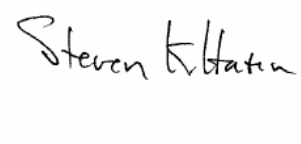
The views and concerns set forth in this Public Commentary are only those of the Corporations Committee. As such, they have not been adopted by the State Bar's Board of Governors, its overall membership, or the overall membership of the Business Law Section, and are not to be construed as representing the position of the State Bar of California. **Membership in the Business Law Section, and on the Committee, is voluntary and funding for activities of them, including all legislative activities, is obtained entirely from voluntary sources. There are currently more than 9,500 members of the Business Law Section.**



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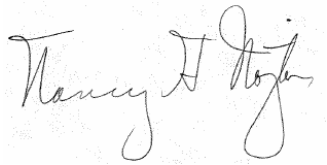
Co-Chair



Nancy H. Wojtas
Co-Chair

Drafting Committee*

Keith Paul Bishop, Esq.
Buchalter, Nemer, Fields & Younger
895 Dove Street
Newport Beach, CA 92660
(949) 760-1121
kbishop@buchalter.com

Nancy H. Wojtas, Esq.
Cooley Godward LLP
Five Palo Alto Square
Palo Alto, CA 94306
(650) 843-5819
nwojtas@cooley.com

Steven K. Hazen, Esq.
Davis Wright Tremaine LLP
865 South Figueroa Street
Los Angeles, CA 90017
(213) 633-6818
skhazen@dwt.com

Daniel J. Weiser, Esq.
Wilson Sonsini Goodrich & Rosati PC
650 Page Mill Road
Palo Alto, CA 94304
(650) 496-4306
dweiser@wsgr.com

The State Bar of California Business Law Section
Corporations Committee Members

As of the date of this Public Commentary, the Corporations Committee is composed of the members shown below, not all of whom necessarily endorse each and every conclusion or view expressed in this Public Commentary. Taken as a whole, however, it reflects a consensus of the members of the Corporations Committee.

Steven K. Hazen, Co-Chair
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Vice-Chair, Education
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Brian D. McAllister
Vice-Chair Communications
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Brian A. Lebrecht
Cynthia Ribas
William R. Sawyers
Lemoine Skinner, III
Suzanne L. Weakley
Brian M. Wong

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NOTES:

1 *Swidler & Berlin v. United States*, 524 U.S. 399, at 403 (1998). Although Justices O'Connor, Scalia and Thomas filed a dissent, it was limited to the question of whether the attorney-client privilege survives the death of the client. Even these three dissenting Justices, however, supported the fundamental nature of the privilege and the role it plays in our system of justice:

> The attorney-client privilege promotes trust in the representational relationship, thereby facilitating the provision of legal services and ultimately the administration of justice. See *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981). The systemic benefits of the privilege are commonly understood to outweigh the harm caused by excluding critical evidence.

Id., at 412. The dissent also appears to recognize the fact that clients have an interest in confidentiality which extends beyond application of the attorney-client privilege: "I agree that a deceased client may retain a personal, reputational, and economic interest in confidentiality." *Id*.

2 *People v. Superior Court*, 25 Cal. 4th 703, at 715 (2001).

3 Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, Exchange Act Release No. 44969, at n. 3 (October 23, 2001). Indeed, the SEC's own Rules of Practice recognize the importance of the SEC's ability to obtain confidential counsel. Rules 230(b)(1)(i) and (ii) permit the SEC to withhold the production of documents that are either privileged or are other attorney work product that will not be offered as evidence.

4 Certain of those matters have been addressed in the Corporations Committee's letter to the Staff of the SEC dated August 13, 2003. The Corporations Committee has also submitted a letter to the IRS earlier this year commenting on regulations adopted by it requiring attorneys to prepare, maintain and furnish informational lists regarding client matters in certain circumstances. Copies of each of those letters are available at the Committee's website: http://www.calbar.org/buslaw/corporations.

5 Notwithstanding the statements of the SEC in the 21(a) Report, the SEC's Form 1662 ("Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to a Commission Subpoena") provides the following disclosure to persons requested to provide information voluntarily: "There are no direct sanctions and thus *no direct effects* for failing to provide all or any part of the requested information." (emphasis added)

6 U.S. Attorney's Manual, Title 9, Section 162 at VI.B (these guidelines are often referred to as the "Thompson Memorandum" as they were originally distributed as an attachment to a memorandum from Deputy Attorney General Larry G. Thompson dated January 20, 2003).

7 For example in *U.S. v. DiStefano,* (S.D.N.Y. 2001) Case. No. S2 98 Cr. 1316 (RWS), a registered representative of a broker-dealer submitted to a nine-hour deposition by the SEC. Subsequently, the U.S. Attorney indicted Mr. DiStephano for conspiracy to commit securities, mail and wire fraud and securities fraud.

8 The SEC uses Form 1662 when giving notice to persons who are requested to supply information or to persons who are directed to supply information pursuant to a subpoena. Form 1662 does not acknowledge the potential of a shareholder civil action and instead somewhat incompletely states: "Information you give may be used against you in any federal, state, local or foreign administrative, civil or criminal proceeding *brought by the SEC or any other agency.*" (emphasis added).

9 SEC Form 1662.

10 "Second, we are not adopting any rule or making any commitment or promise about any specific case; nor are we in any way limiting our broad discretion to evaluate every case individually, on its own particular facts and circumstances." 21(a) Report.

11 Citing *U.S. v. Morton Salt Co.*, 338 U.S. 632 (1950), the SEC takes the position that it does not need "probable cause" to conduct an investigation, rather it has the power of inquisition. Memorandum of the SEC in Support of its Application for Orders to Show Cause, for an *In Camera* Review, and Requiring Obedience to Subpoena. *U.S. Securities and Exchange Comm'n v. Lay*, Civil Action No. 1:03 MS 01962 (RCL) (D.D.C., September 29, 2003).

12 In *Page v. U.S.*, 884 F.2d 300 (7th Cir. 1989), Judge Easterbrook provided a standard description of the "prisoners' dilemma":

> Students of strategy and bargaining cut their teeth on the game of Prisoners' Dilemma. Two prisoners, unable to confer with one another, must decide whether to take the prosecutor's offer: confess, inculpate the other, and serve a year in jail, or keep silent and serve five years. If the prisoners could make a (binding) bargain with each other, they would keep silent and both would go free. But they can't communicate, and each fears that the other will talk. So both confess. Studying Prisoners' Dilemma has led to many insights about strategic interactions.

13 Waiver of client confidentiality would be the dominant strategy for each of the corporations in this position because it outperforms the alternative, no matter what the other corporations do. What those students of strategy and bargaining referenced by Judge Easterbrook identify as the "Nash equilibrium" would thus be associated with clients waiving the privilege. Interestingly, the defendant's lawyer in *Page* apparently missed this point and it became the basis of the defendant's appeal.

14 *See*, *City and County of San Francisco v. Superior Court*, 37 Cal. 2d 227, at 235 (1951) ("The privilege is given on grounds of public policy in the belief that the benefits derived therefrom justify the risk that unjust decisions may sometimes result from the suppression of relevant evidence").

15 Keating, Muething & Klekamp, 47 SEC 95, at 109 (1979) (dissenting opinion of Commissioner Roberta S. Karmel).

16 The Corporations Committee notes that the abundant case law on the right to counsel under the Sixth Amendment would provide additional support for (and arguments in favor of) preserving the confidentiality characteristics of the attorney-client relationship. Indeed, any judicial proceedings contesting regulatory provisions or enforcement practices which weakened the practical effects of that characteristic almost certainly would include extensive citation to such authorities. That is, however, beyond the scope of this Public Commentary as being unnecessary to highlight the authorities and arguments more specifically focused in that confidentiality characteristic.

17 5 U.S.C. § 555(b) ("A person compelled to appear in person before an agency or representative thereof is entitled to be accompanied, represented, and advised by counsel or, if permitted by the agency, by other qualified representative."). The SEC's Form 1662 ("Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information to a SEC Subpoena") provides:

> You have the right to be accompanied, represented, and advised by counsel of your choice. Your counsel may advise you before, during and after your testimony; question you briefly at the conclusion of your testimony to clarify any of the answers you give during your testimony; and make summary notes during your testimony solely for your use. If you are accompanied by counsel, you may consult privately.

18 *Mitchell v. Superior Court,* 37 Cal. 3d 591, at 599 (1984).

19 *People ex rel. Dept. of Corporations v. SpeeDee Oil Change Systems, Inc.*, 20 Cal. 4th 1135, at 1146 (1999).

20 Francis Bacon, *Essayes - Of Counsel* (emphasis added).

21 *D.I. Chadbourne, Inc. v. Superior Court,* 60 Cal. 2d 723, at 736 (1964), quoting Simon, *The Attorney-Client Privilege as Applied to Corporations*, 65 Yale L. J. 953, at 990 (1956).

22 *See*, American Institute of Certified Public Accountants, Code of Professional Conduct, Section 55 – Article IV ("A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public practice should be independent in fact and appearance when providing auditing and other attestation services.").

23 *In the Matter of Touche, Niven, Bailey & Smart,* 37 S.E.C. 629, at 670-671 (1957).

24 American Institute of Certified Public Accountants, Code of Professional Conduct, Section 53.01 – Article II.

25 15 U.S.C. §§ 77aa(25) and (26) and 15 U.S.C. § 78q.

26 15 U.S.C. §§ 78l and 78m; 15 U.S.C. §§ 79e(b), 79j, and 79n; 15 U.S.C. §§ 80a-8 and 80a-29; and 15 U.S.C. § 80b-3(c)(1).

27 Pub. L. 107-204, 116 Stat. 745 (2002).

28 New sub-section (g) prohibits a number of non-audit services; new sub-section (h) requires pre-approval of permitted non-audit services; new subsection (i) pertains to pre-approval by an issuer's audit committee; new sub-section (j) establishes mandatory rotation for an auditor's lead and concurring partners; new sub-section (k) requires the auditor to report certain information to the audit committee; and new sub-section (l) addresses certain conflicts of interest.

29 *United States v. Arthur Young & Co.*, 465 U.S. 805, at 817-818 (1984) (emphasis in original). However, even accountants do not hold a limitless responsibility to the public. The California Supreme Court has held that an independent auditor "owes no general duty of care regarding the conduct of an audit to persons other than the client. An auditor may, however, be held liable for negligent misrepresentations in an audit report to those persons who act in reliance upon those misrepresentations in a transaction which the auditor intended to influence". *Bily v. Arthur Young & Co.*, 3 Cal. 4th 370, at 376 (1992).

30 See text and note at footnote 22.

31 The advocacy role of California attorneys is, of course, constrained by (among other things) Rule 3-210 of the California Rules of Professional Conduct which provides: "A member shall not advise the violation of any law, rule, or ruling of a tribunal unless the member believes in good faith that such law, rule, or ruling is invalid. A member may take appropriate steps in good faith to test the validity of any law, rule, or ruling of a tribunal." Further, the State Bar Act requires attorneys "to counsel or maintain those actions, proceedings, or defenses only as appear to him or her legal or just, except the defense of a person charged with a public offense." Cal. Bus. & Prof. Code § 6068(c). Those and other similar limits do not, however, make the attorney *independent* of the client.

32 This distinction between accountants and attorneys has also been recognized by courts in states other than California:

> Unlike an attorney who is required to zealously represent a client's position in an adversarial setting, an independent auditor who is hired to give an opinion on a client's financial statements must do so with an independent impartiality which contemplates reliance upon the audit by interests other than the entity upon which the audit is performed. See 1 American Inst. of Certified Pub. Accountants, Professional Standards § 220.02. Rather than acting as an advocate with an undivided duty of loyalty owed a client, an independent auditor performs a different function.

KPMG Peat Marwick v. Nat'l Union Fire Ins. Co., SC96413 (Fla. S. Ct. 2000) (footnotes omitted).

> The attorney-client relationship is personal in both nature and objective. In contrast, from its inception the auditor-client relationship exists not merely for the

benefit of the client, but also for the benefit of the shareholders and the public with whom the client may transact business.

Standard Chartered PLC v. Price Waterhouse, 190 Ariz. 6, at 17 (1996).

33 *United States v. Arthur Young & Co.*, 465 U.S. 805, at 817 (1984):

The *Hickman* [*Hickman v. Taylor*, 329 U.S. 495 (1947)] work-product doctrine was founded upon the private attorney's role as the client's confidential adviser and advocate, a loyal representative whose duty it is to present the client's case in the most favorable possible light. An independent certified public accountant performs a different role.

34 *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983).

35 *Goodman v. Kennedy,* 18 Cal. 3d 335, at 344 (1976) (footnote omitted).

36 Section 201(g) of the Sarbanes-Oxley Act. The SEC has defined "legal services" as providing "any service to an audit client that, under circumstances in which the service is provided, could be provided only by someone licensed, admitted, or otherwise qualified to practice law in the jurisdiction in which the service is provided". Regulation S-X, 17 C.F.R. § 210.2-01(c)(4)(ix).

37 Cal. Bus. & Prof. Code § 6068(e).

38 *People v. Kor,* 129 Cal. App. 2d 436, at 447 (1954) (emphasis added). It is worth noting that the third Justice on the panel concurred in the opinion of the court and in the judgment (as did Justice Shinn) but also specifically concurred in the comments of Justice Shinn. The final observation of Justice Shinn reverberates today: "This is not intended as a criticism of the action of the attorneys. It is, however, a suggestion to any and all attorneys who may have the misfortune to be confronted by the same or a similar problem." *Id*.

39 Cal. Evid. Code § 955 ("The lawyer who received or made a communication subject to the privilege under this article shall claim the privilege whenever he is present when the communication is sought to be disclosed and is authorized to claim the privilege under subdivision (c) of Section 954").

40 Cal. Code Regs., tit. 16, § 54.1.

41 The statutory rules governing the attorney-client privilege are set forth in Division 8, Article 3 of the California Evidence Code (commencing with Section 950). Fed. Rules of Evidence 501.

42 *Couch v. United States*, 409 U.S. 322, at 335 (1973).

43 SEC Release No. 33-8183; 34-47265; 35-27642; IC-25915; IA-2103; FR-68 (January 28, 2003).